

## Internal Revenue Service

Number: **201519011**

Release Date: 5/8/2015

Index Number: 9100.00-00, 9100.22-00,  
108.01-00

Department of the Treasury

Washington, DC 20224

Third Party Communication: None

Date of Communication: Not Applicable

Person To Contact:

, ID No.

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Refer Reply To:

CC:ITA:4

PLR-132946-14

Date:

January 15, 2015

TY:

### Legend

Taxpayers =

Year 1 =

Year 2 =

Year 3 =

Date 1 =

Date 2 =

Firm 1 =

Firm 2 =

Firm 3 =

Bank =

x =

Y =

Dear :

This letter responds to your request for an extension of time under § 301.9100-3 of the Procedure and Administration Regulations to make an election under § 108(c)(3)(C) of the Internal Revenue Code. Specifically, you have requested an extension of time to make an election under § 108(c)(3)(C) of the Code and § 1.108-5(b) of the Income Tax Regulations, to exclude income resulting from the discharge of qualified real property business indebtedness and to reduce the basis of depreciable real property, effective for Taxpayer's Year 1 federal income tax return.

### Facts

Taxpayers use the cash method of accounting and have a calendar year as an annual accounting period. Taxpayers were a combined x percent owner of Y, which owned a

residential rental property that was subject to a short sale in Year 1. After the short sale and relinquishment of the property, Y ceased operations as of Date 1.

The short sale occurring in Year 1 created cancellation of debt (COD) income to Y, and the COD income was reported on a Form 1099-C, *Cancellation of Debt*, issued from Bank.

In Year 2, Y relied on a tax professional at Firm 1 to prepare Y's Year 1 Form 1065, *U.S. Return of Partnership Income*. However, neither Form 1065 nor the corresponding Schedule K-1, *Partner's Share of Income, Deductions, Credits, etc.*, indicated that the COD related to qualified real property business indebtedness.

Taxpayers relied on a different tax professional at Firm 2 to prepare their Year 1 Form 1040, *U.S. Individual Income Tax Return*. Firm 2 was unaware of the nature of the Taxpayers' COD income and, thus, failed to advise Taxpayers about the opportunity to make the election under § 108(c)(3)(C) of the Code and § 1.108-5(b) of the regulations.

Taxpayers timely filed the Year 1 federal income tax return (including the extension) on Date 2 and set up an Installment Agreement using Form 9465, *Installment Agreement Request*. Taxpayers represent that they have been current on all payments since the time of filing.

In Year 3, a different tax professional at Firm 3 reviewed Taxpayers' Year 1 Form 1040, and discovered that Taxpayers could have elected to exclude the COD income. However, the time allowed for filing the election had expired. Taxpayer and the tax professionals at Firm 2 and Firm 3 have submitted affidavits consistent with the above facts.

Taxpayers represent that granting relief under § 301.9100-3 will not result in a lower tax liability in the aggregate for all years to which the election applies than the taxpayer would have had if the election had been timely made.

### Applicable Law

Section 108(a)(1)(D) provides that gross income does not include any amount that would be included in gross income by reason of the discharge of indebtedness if, in the case of a taxpayer other than a C corporation, the indebtedness discharged is qualified real property indebtedness.

Section 108(c)(1) provides that the amount excluded from gross income is applied to reduce basis of the depreciable real property of the taxpayer. Section 108(c)(3)(C) requires a taxpayer to make an election to exclude COD income under § 108(a)(1)(D).

Section 108(c)(2)(A) provides that the amount excluded under § 108(a)(1)(D) for any qualified real property business indebtedness does not exceed the excess (if any) of (i) the outstanding principal amount of such indebtedness (immediately before the discharge), over (ii) the fair market value of the real property described in paragraph (3)(A) (as of such time), reduced by the outstanding principal amount of any other qualified real property business indebtedness secured by such property (as of such time).

Section 108(c)(2)(B) provides that the amount excluded under 108(a)(1)(D) does not exceed the aggregate adjusted bases of depreciable real property (determined after any reductions under § 108(b) and § 108(g)) held by the taxpayer immediately before the discharge (other than depreciable real property acquired in contemplation of such discharge).

Section 108(d)(6) provides that in the case of a partnership, § 108(a) and § 108(c) apply at the partner level.

Section 1.108-5(b) provides that the election under § 108(c)(3)(C) is made on the timely-filed (including extensions) Federal income tax return for the taxable year in which the taxpayer has discharge of indebtedness income that is excluded from gross income under § 108(a). The election is made on a completed Form 982, *Reduction of Tax Attributes Due to Discharge of Indebtedness (and Section 1082 Basis Adjustment)*, in accordance with that Form and its instructions.

Sections 301.9100-1 through § 301.9100-3 provide the standards that the Commissioner will use to determine whether to grant an extension of time to make a regulatory election. Section 301.9100-3(a) provides that requests for extensions of time for regulatory elections (other than automatic extensions covered in § 301.9100-2) will be granted when the taxpayer provides evidence (including affidavits) to establish that the taxpayer acted reasonably and in good faith, and granting relief will not prejudice the interests of the Government.

Under § 301.9100-3(b), a taxpayer is deemed to have acted reasonably and in good faith if the taxpayer requests relief before the failure to make the regulatory election is discovered by the Service, or reasonably relied on a qualified tax professional, and the tax professional failed to make, or advise the taxpayer to make, the election. A taxpayer will not be considered to have reasonably relied on a qualified tax professional if the taxpayer knew or should have known that the professional was not competent to render advice on the regulatory election or aware of all the relevant facts.

In addition, § 301.9100-3(b)(3) provides that a taxpayer is deemed to have not acted reasonably and in good faith if the taxpayer—

- (i) seeks to alter a return position for which an accuracy-related penalty has been or could be imposed under § 6662 at the time the taxpayer requests relief, and the new position requires or permits a regulatory election for which relief is requested;
- (ii) was fully informed of the required election and related tax consequences, but chose not to file the election; or
- (iii) uses hindsight in requesting relief. If specific facts have changed since the original deadline that make the election advantageous to a taxpayer, the Service will not ordinarily grant relief.

Section 301.9100-3(c)(1) provides that the Commissioner will grant a reasonable extension of time to make the regulatory election only when the interests of the Government will not be prejudiced by the granting of relief.

Section 301.9100-3(c)(1)(i) provides that the interests of the Government are prejudiced if granting relief would result in a taxpayer having a lower tax liability in the aggregate for all taxable years affected by the election than the taxpayer would have had if the election had been timely made (taking into account the time value of money).

Section 301.9100-3(c)(1)(ii) provides that the interests of the Government are ordinarily prejudiced if the taxable year in which the regulatory election should have been made or any taxable year that would have been affected by the election had it been timely made are closed by the period of limitation on assessment under § 6501(a) before the taxpayer's receipt of a ruling granting relief under this section.

Based on the information submitted by Taxpayers, we conclude that (1) Taxpayers acted reasonably and in good faith under § 301.9100-3(b), and (2) the interests of the Government will not be prejudiced by the granting of relief under § 301.9100-3(c).

### Conclusion

Accordingly, based solely on the information submitted and the facts represented in the ruling request, and provided that the Operating Division Director does not determine that Taxpayer is subject to an accuracy-related penalty under § 6662, we grant Taxpayers an extension of 45 days from the date of this letter ruling to file an amended return to make the election under § 108(c)(3)(C) and § 1.108-5(b). The election is to be made on Form 982.

The ruling contained in this letter is based upon the information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. Although this office has not verified any of the material

submitted in support of the request for the ruling, that material is subject to verification on examination.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. Specifically, this letter does not rule on whether the income at issue is properly treated as cancellation of indebtedness income under § 61(a)(12). In addition, except for the relief granted to make a late election, this letter also does not rule on whether the income in fact qualifies for exclusion from income under any provision of § 108 (including § 108(a)(1)(D)).

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Enclosed is a copy of the letter showing the deletions proposed to be made when it is disclosed under § 6110. If you have any questions concerning this matter, please contact the individual whose name and telephone number appear at the beginning of the letter.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, a taxpayer filing a return electronically may satisfy this requirement by attaching a statement to the return that provides the date and control number of the letter ruling.

Sincerely,

Michael J. Montemurro  
Chief, Branch 4  
Office of Associate Chief Counsel  
(Income Tax & Accounting)